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April 29, 2002

Via Hand Delivery

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W., Room TW-B204
Washington, D.C. 20554
c/o 236 Massachusetts Avenue, N.E.
Suite 110
Washington, D.C. 20002-4913

Re: *Applications for Consent to the Transfer of Control of Licenses from Comcast Corporation and AT&T Corporation to AT&T Comcast Corporation*, MB Docket No. 02-70

Dear Ms. Dortch:

Enclosed for filing in the above-captioned proceeding are the original and four (4) copies of the Comments of SBC Communications Inc.

Please call me at 202-326-7968 if you have any questions. Thank you for your assistance.

Sincerely,

Colin S. Stretch

Enclosures

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of Applications for Consent to the Transfer of Control of Licenses COMCAST CORPORATION and AT&T CORP., Transferors, To AT&T COMCAST CORPORATION, Transferee.	)	MB Docket No. 02-70

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April 29, 2002

EXECUTIVE SUMMARY

Even viewed against the backdrop of unprecedented consolidation in the cable industry, the proposed merger of AT&T and Comcast is stunning. AT&T and Comcast (the "Applicants") are the first and third largest cable operators in the country. Together (setting to one side AT&T's 25-percent share of Time Warner), they already provide video programming to close to one-third of the nation's MVPD subscribers.

Standing alone, such broad coverage might not threaten the public interest. After all, the merger would eliminate little or no actual competition, since the Applicants – like the remainder of the cable industry – have historically refused to overbuild other cable territories, even though they have access to the content that could make such an effort worthwhile. But, critically, the Applicants' vast video bottleneck does not stand alone. AT&T and Comcast both have tentacles reaching far upstream into vertically related businesses, providing control over content that MVPD providers wishing to challenge cable's hegemony need to compete. And, make no mistake, each of the merging parties has a well-established history of abusing that control to disadvantage competitors. Thus, for example, Comcast has steadfastly refused to provide DBS providers with access to its regional sports programming in certain areas, instead performing an end-run around the Commission's program access rules and thereby limiting its competitors' growth to well below the national average. AT&T has likewise refused to provide its content aggregation service – known as "Headend in the Sky," or "HITS" – to competing MVPDs that so much as cross a right-of-way in its service area.

If approved as proposed, the merger would permit these companies to continue this anticompetitive conduct, but on a far larger stage. Indeed, the Commission has already acknowledged that, combined with its vertical content interests, the scale of AT&T's cable operations *alone* threatens "competition and diversity in the delivery of programming to consumers." It necessarily follows that uniting AT&T with Comcast's expansive properties and vertical interests poses a far more substantial threat to MVPD competition.

The threat to broadband Internet access is even more severe. The dominant cable incumbents already control close to 70 percent of broadband Internet access subscribers, and their lead is growing. The market is nascent, moreover, and – particularly in light of its network characteristics – it is highly susceptible to vertical foreclosure. This merger would make the significant cable broadband players both more powerful and less numerous, and thus raise the distinct possibility that the merged company – acting either alone or in concert with but a few cable brethren – will be able to tip the market irretrievably toward the cable platform.

This danger is particularly problematic because the cable platform's chief competitor – DSL-based access provided by incumbent LECs – continues to be shackled by one-sided, onerous regulatory requirements that severely distort the competitive process. Though ILECs as a group collectively provide service to less than a third of broadband subscribers, they remain subject not only to a vast array of access requirements – including, among others, unbundling spectrum, collocation, and loop conditioning – but also the continuing threat of additional obligations. What is more, the largest of the ILECs have been forced as a condition of recent mergers to carve out their advanced services operations into separate affiliates, purportedly to make these requirements more effective. The cable incumbents face none of these obligations, and neither AT&T nor Comcast has made a meaningful commitment to provide ISP access to its broadband networks – AT&T's confidential, eleventh-hour deals being all the more insufficient in light of its three-year-old pledge to provide nondiscriminatory access to multiple ISPs. AT&T and Comcast accordingly enjoy an artificial regulatory advantage that distorts the competitive process and renders DSL an insufficient competitive counterbalance to the market power the Applicants will obtain as a result of this merger.

To offset these undeniable harms, the Applicants once again trot out the familiar claim that the transaction will further the development of facilities-based voice competition in the residential market. But, for one thing, this claim runs counter to AT&T's claim in the *Triennial Review* proceeding that cable telephony is not viable, and that CLECs continue to require unbridled access to ILEC facilities to serve the residential market. Moreover, for years AT&T has been claiming that its expertise *as a phone company* would turn its cable properties into robust voice competitors. Now it claims that jettisoning that expertise – and uniting instead with a company that has steadfastly committed *not* to "touch[] circuit-switched telephony with a 10-foot pole" – is required to achieve that same result. In light of the Applicants' own characterizations of the prospects of cable telephony, it is difficult to take their claims seriously.

The Applicants have thus fallen well short of establishing, as they must, that the benefits of the proposed transaction outweigh its harms. The Commission may accordingly approve the transaction only if it imposes conditions that would mitigate the harms threatened, and encourage the benefits claimed.

In the video business, that means requiring AT&T to divest not only its interest in Time Warner Entertainment – as the Applicants concede they must do – but also its interest in HITS. In addition, the Commission must require the Applicants to license all content in a nondiscriminatory manner regardless of the medium used to deliver programming, and thereby prevent them from withholding valuable content from competing video providers.

In broadband, the Commission must commit – in the numerous rulemaking proceedings that are now underway – to deregulate ILECs and permit them to compete head-to-head with cable, without the disincentives and additional costs that flow as a direct consequence of the Commission's asymmetric rules. Unless ILECs are free to compete with cable on an equal regulatory footing, the Commission cannot rely on them to mitigate the competitive threat posed by the dominant cable incumbents.

It is not enough, however, for the Commission merely to *intend* to free ILECs from burdensome regulation. Each day that the regulatory imbalance remains in place, the cable incumbents can further cement their enormous lead in broadband Internet access. And they may further leverage that lead to strike deals with content providers and others that disfavor DSL and other competitors. SBC has always been and continues to be firmly committed to the principle that all broadband services should be governed by the marketplace and not by regulatory fiat. But the fact remains that this is not the situation in place today, and interim measures are necessary to ensure that cable does not transform its vast head-start into perpetual market dominance. To permit the Applicants to continue to exploit this imbalance – even for a period as short as a year – is potentially to stifle the development of competition in broadband permanently.

The Commission must accordingly hold the transaction in abeyance until it puts in place a coherent, uniform broadband regulatory framework that eliminates ILECs' disincentives to invest in broadband, and permits them to compete head-to-head with the Applicants. Until it does so – and removes the disincentives to investment that now plague ILECs' participation in the broadband market – the merger cannot be allowed to proceed.

If the Commission is unwilling to hold the merger in abeyance pending its articulation of a uniform broadband regulatory framework, at the very least it must impose conditions on the transaction to protect the public interest. That means imposing – in *this* docket – obligations on AT&T/Comcast that mirror the obligations that the Commission has imposed on ILECs. SBC continues to believe that any conditions attached to license transfer applications should be narrowly tailored to address precise, identifiable harms that are the direct result of the merger. The open access conditions proposed here amply satisfy that test. Indeed, to allow this merger to close without leveling the broadband regulatory and competitive field will only exacerbate the already substantial competitive and market share advantages held by cable modem providers.

In voice, the Commission must likewise take steps to encourage facilities-based competition. SBC does not here propose that the Commission continue its approach – applied in other mergers of comparable scale – of adopting particular investment or entry requirements. Instead, the Commission should simply put in place rules that would encourage the Applicants to live up to their pledge to deploy new telephony facilities. In particular, the Commission should forbid the merging parties from obtaining unbundled network elements – and particularly full platforms of such elements – in any geographic area where those companies provide cable service today or in the future. Such a condition will foster facilities-based competition by requiring a combined AT&T/Comcast to utilize its own facilities to compete with ILECs, the very pro-competitive advantage cited by the Applicants to support the merger.

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In the Matter of Applications for Consent to the Transfer of Control of Licenses COMCAST CORPORATION and AT&T CORP., Transferors, To AT&T COMCAST CORPORATION, Transferee.	)	MB Docket No. 02-70

SBC Communications Inc. ("SBC") respectfully submits these comments in response to the Commission's public notice in the above-referenced docket.

The proposed merger marks the culmination of a decade of unprecedented consolidation in the cable industry. AT&T is already the nation's largest cable operator, and it still maintains a substantial attributable interest in Time Warner Entertainment, which owns the nation's second largest cable operator. Comcast is the third largest. Even without Time Warner, the Applicants would be the largest "last mile" provider in the country – an enormous, vertically integrated media conglomerate with extensive interests not only in video and broadband distribution, but also in video programming and broadband content as well.

This unprecedented combination of content and distribution poses substantial threats to the video distribution and, by extension, broadband Internet access markets. Consumers are increasingly relying on bundled video and data service, and "[w]ith almost 70 percent of U.S. households having cable TV, the MSOs could easily convert these customers to cable modem subscribers."[1] To attempt to compete with cable for these customers, SBC has recently teamed with EchoStar to provide a video and broadband bundle.[2] Yet, if this merger is approved as proposed, the viability of that offering will be in serious jeopardy. A combined AT&T/Comcast would have the incentive and the ability to foreclose competition in both the video and Internet content markets, and thereby diminish the ability of other platforms to compete on an equal footing.

To offset these undeniable public interest harms, moreover, the Applicants rely upon a single, wholly unsubstantiated claim: that the merger will facilitate increased deployment of cable telephony. Yet, barely three weeks ago, AT&T filed approximately 1,000 pages of comments and supporting declarations dedicated in large part to the proposition that widespread facilities-based competition in the residential market is unlikely, and that competitors continue to require complete reliance on ILEC facilities.[3] In light of this obvious duplicity, the Commission can hardly credit these alleged benefits.

The Commission must accordingly take significant steps not only to mitigate the adverse effects of this merger in both multi-channel video programming distribution ("MVPD") and

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[1] Insight Research Corp., Market Research Reports Summary, *DSL vs. Cable Modems: The Future of High-Speed Internet Access 2000-2005*, *at* http://www.insight-corp.com.

[2] *See* Tiffany Kary, *Satellite, DSL Team Up Against Cable*, CNET News.com (Apr. 19, 2002), *at* http://story.news.yahoo.com/news?tmpl=story&cid=70&ncid=738&e=6&u=/cn/20020419/tc_cn/satellite__dsl_team_up_against_cable.

[3] *See, e.g.*, Comments of AT&T Corp. at 58, CC Docket No. 01-338, *et al.* (FCC filed Apr. 5, 2002) ("cable companies in general have been able only gradually to invest in and adopt the technology needed to offer telephony; and limitations on capital and operating experience make it questionable how quickly and comprehensively this particular form of competition will evolve"); *id.* at 12 ("CLECs are serving almost as many residential local telephone customers through UNE-P in New York alone than are served by all the nation's cable operators in the country as a whole.").

broadband Internet access, but also to ensure that the Applicants make good on their promise to rely on their own facilities, rather than ILEC UNEs, to provide local voice service.

Such steps are particularly important in light of the fact that the merger takes place against a backdrop of significant regulatory uncertainty. In video distribution, the Commission's horizontal ownership rules – which in past mergers have served to mitigate concern about foreclosure of video programming content – have been vacated, and the Commission has yet to promulgate new rules to take their place. In broadband, although the Commission is weighing a series of proposals that may eventually provide some coherence to the regulation of competing platforms, it remains the case that the Applicants' chief competition – ILEC-provided DSL – is mired in a web of costly, disparate regulation. Through participation in recent merger proceedings, SBC is familiar with the nature of this Commission's merger review process, and it continues to believe that the scope of that review is often overly expansive. Yet, if the Commission's practice of comprehensive merger review is determined to be appropriate in any case, it is clearly so here, where, in the absence of existing regulations, the merger review process is the critical – if not the only – forum in which to timely address the numerous competitive threats posed.

DISCUSSION

In the wake of the Telecommunications Act of 1996 ("1996 Act"), the Commission has set a high bar for communications companies hoping to merge. "In order to find that a merger is in the public interest," this Commission must "be *convinced* that it will enhance competition."[4]

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[4] Memorandum Opinion and Order, *Applications of NYNEX Corp. and Bell Atlantic Corp. For Consent to Transfer Control of NYNEX Corp. and Its Subsidiaries*, 12 FCC Rcd 19985, 19987, ¶ 2 (1997) ("*Bell Atlantic/NYNEX Order*") (emphasis added); *see also* Memorandum Opinion and Order, *Applications of Ameritech Corp. and SBC Communications Inc. For Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95 and 101 of the Commission's Rules*, 14 FCC Rcd 14712, 14738, ¶ 49 (1999) ("*SBC/Ameritech*

A merger satisfies this standard only if "the harms to competition – *i.e.*, enhancing market power, [or] slowing the decline of market power . . . are outweighed by benefits that enhance competition. If applicants cannot carry this burden, the applications must be denied."[5] The Applicants have fallen well short of meeting that demanding standard.

I. THE MERGER WILL REDUCE COMPETITION IN THE MVPD MARKET.

In 1992, Congress expressly warned that increasing levels of concentration in the cable industry could create "barriers to entry for new programmers and a reduction in the number of media voices available to consumers."[6] In the ensuing ten years, the Commission has witnessed cable industry consolidation on an unprecedented scale. Yet none of those transactions posed as significant a threat to the statutory interests in programming diversity and competition as this latest – and by far the largest – transaction.

Horizontal Concentration and Vertical Foreclosure. The anticompetitive risks of vertical links between distribution and content have long been a concern of competition policy. Congress, the Department of Justice, and the Federal Trade Commission have all acknowledged this as a serious problem. Vertical leveraging was the motivating concern behind two federal Acts (the 1992 Cable Act and the Satellite Home Viewer Improvement Act of 1999) and several consent decrees.[7] Moreover, the D.C. Circuit has expressly endorsed the view that "increases in

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Order").

[5] *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 19987, ¶ 2.

[6] Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, § 2(a)(4), 106 Stat. 1460 ("1992 Cable Act"); *see* Third Report and Order, *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992*, 14 FCC Rcd 19098, 19118-19, ¶ 51 (1999) ("*Horizontal Ownership Third Report and Order*").

[7] *See United States v. Primestar Partners, L.P.*, 1994-1 Trade Cas. (CCH) ¶ 70,562 (S.D.N.Y. 1994); Proposed Final Judgment and Competitive Impact Statement, *United States v. Tele-Communications, Inc.*, 59 Fed. Reg. 24723, 24727 (May 12, 1994); Decision and Order, *Time Warner Inc., a Corporation; Turner Broadcasting System, Inc., a Corporation; Tele-Communications, Inc., a Corporation; and Liberty Media Corporation, a Corporation*, Docket

the concentration of cable operators threaten[] diversity and competition in the cable industry."[8] Thus, although the court vacated and remanded the Commission's horizontal ownership limits for lack of a sufficient evidentiary record, it left intact – and indeed reaffirmed – the Commission's mandate under section 613(f)(1) of the Communications Act to guard against undue concentration in the cable industry. That mandate requires the Commission to *ensure* that "no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer."[9]

There can be little doubt that, if the Commission allows this merger to proceed as proposed, it will have exactly that effect. As noted at the outset, standing alone, AT&T and Comcast are the first and third largest cable operators in the country.[10] According to their own Public Interest Statement, they will provide video programming to approximately 30 percent of all MVPD subscribers.[11] And that is only the half of it. As the Applicants appear to concede (*see* Public Interest Statement at 61), AT&T's 25-percent stake in Time Warner Entertainment renders the proposed merger a nonstarter under the governing rules and regulations. And while AOL Time Warner has recently professed interest in buying AT&T's interest in TWE, a mere intention to divest – without any enforceable commitment or condition – is hardly sufficient to permit approval of this unprecedented transaction.

No. C-3709 (FTC Feb. 3, 1997).

[8] *Time Warner Entm't Co. v. FCC*, 240 F.3d 1126, 1130 (D.C. Cir. 2001) (internal quotation marks omitted).

[9] 47 U.S.C. § 533(f)(2)(A).

[10] *See* Eighth Annual Report, *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 17 FCC Rcd 1244, 1341, Table C-3 (2002) ("*Eighth Annual Video Report*").

[11] Public Interest Statement at 50.

Yet even without Time Warner, the proposed transaction seriously threatens MVPD competition. As the Commission has previously acknowledged, a subscribership base on the order proposed by the Applicants can severely impact "competition and diversity in the delivery of video programming to consumers."[12] That is so because "[s]tart-up video programmers need to reach a critical level of subscribership quickly in order to achieve long-term financial viability." *AT&T/MediaOne Order*, 15 FCC Rcd at 9841, ¶ 51. If one particular cable operator – or more than one, acting in concert – controls access to a sufficient number of subscribers, it may be in a position "to deal a programmer a death blow," and thereby reduce competition for programming content. *Time Warner*, 240 F.3d at 1131; *see* Declaration of Robert H. Gertner ¶ 20 ("Gertner Decl.") (Attachment A hereto).

A combined AT&T/Comcast could have precisely that effect. Indeed, the Commission has already concluded that AT&T's subscriber base, standing alone, creates "significant bargaining power." *AT&T/MediaOne Order*, 15 FCC Rcd at 9841, ¶ 51. It did so, moreover, while of the view that 15 million MVPD subscribers "is the minimum number necessary to give a video programmer a reasonable chance of long-term success." *Id.* at 9842, ¶ 55 (citing *Horizontal Ownership Third Report and Order*, 14 FCC Rcd at 19117-18, ¶¶ 48-49). More recent evidence supports the view that, at least in some cases, the Commission significantly *under*estimated the number of subscribers necessary to support new programming, and that in fact 25 million subscribers is the minimum number necessary for long-term viability.[13] It

[12] Memorandum Opinion and Order, *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from MediaOne Group, Inc. to AT&T Corp.*, 15 FCC Rcd 9816, 9840-41, ¶ 50 (2000) ("*AT&T/MediaOne Order*").

[13] *See AOL, NBA Need 25 Million Subscribers to Launch Channel*, Reuters (Apr. 12, 2002) ("The new cable channel AOL Time Warner Inc. and the National Basketball Association plan to launch later this year will only become a reality if it reaches 25 million subscribers from its first day, NBA Commissioner David Stern said."). Although the D.C. Circuit vacated the horizontal ownership limit, it did not question the Commission's view that 15 million subscribers were necessary to support new programming. *Time Warner*, 240 F.3d at 1131.

necessarily follows that vastly expanding AT&T's subscribership base by combining it with Comcast's creates a serious threat to competition and diversity in video programming.

As the Commission recognized in the *AT&T/MediaOne Order*, moreover, "recent consolidation in the MVPD industry" exacerbates these concerns. 15 FCC Rcd at 9843, ¶ 57. AT&T's cable operations were created by consolidations with MediaOne and TCI, which were themselves outgrowths of years of consolidation of at least 15 separate cable operators.[14] Comcast's current operations were similarly created over a number of years through the consolidation of at least eight separate cable operators, including Jones Intercable and Lenfest Communications.[15] The current Adelphia cable operations were created through the consolidation of at least 25 separate cable operators, including acquisitions of Century Communications, Harron Communications, and G.S. Communications.[16] Charter includes what

[14] *See American Cablesystems Corporation and Continental Cable to Merge*, PR Newswire (Oct. 14, 1987); *Continental Cablevision Sets $1.4 Billion Deal*, United Press Int'l (Nov. 22, 1994); J. Estrella, *SouthCoast's First Wave of Cable Changes Hits Today*, SouthCoast Today (Aug. 7, 1997); B. Mattson, *Continental Rides to Top with Zeuli*, Minneapolis-St. Paul City Bus., sec. 1, at 15 (Dec. 22, 1995); New Paradigm Resources Group, Inc., *CLEC Report 1998*, MediaOne, at 3 (9th ed. 1997); M. Ricciutu, *AT&T, MediaOne Merger a Done Deal*, CNET News.com (June 15, 2000), *at* http://news.cnet.com/news/0-1004-200-2082335.html; T. Gauntt, *Dallas Radio Chain Makes Offer for Ailing KKSN*, Bus. J. – Portland (Apr. 25, 1988); K. Bulkley, *WTCI Takes New Direction, Moves into Cable Business*, Denver Bus. J., sec. 1, at 10 (Oct. 26, 1987); *Telecommunications Financial Results*, Bus. Wire (Mar. 29, 1988); F. Danzig, *Media's Fastest-Rising Star, Cable, Soars 23.9%*, Advertising Age, at S-14 (June 26, 1989); K. Oberlander, *UA Board Mulls Offer From TCI*, Electronic Media, at 3 (May 6, 1991); *TCI Announces Agreement on Merger with United Artists*, Associated Press (June 7, 1991); TCI, 1994 10-K (SEC filed Mar. 31, 1995); C. Moozakis, *AT&T, TCI Complete Merger*, Internet Week (Mar. 9, 1999), *at* http://www.internetwk.com/news0399/news030999-11.htm.

[15] Comcast, *About Us: Key Events*, *at* http://www.comcast.com/defaultframe.asp?section=about_us&SubSection=au-key_events.

[16] Adelphia Communications, Inc., 2001 10-Q (SEC filed May 15, 2001); J. Maclain, *TV Delivery Contest Rages*, Ventura County Star, at D1 (July 22, 2001); Adelphia Communications, Inc., 10-Q (SEC filed Nov. 14, 2000); Adelphia Communications, Inc., 1998 10-KT (SEC filed May 25, 1999); Adelphia Communications, Inc., 10-Q (SEC filed Nov. 15, 1999); Adelphia Communications, Inc., 1997 10-K (SEC filed June 26, 1998); Adelphia Communications, Inc., 1996 10-K (SEC filed June 20, 1997); Adelphia Communications, Inc., 1996 10-Q (SEC filed

were formerly at least 20 separate cable operators.[17] The consolidation of at least 15 separate cable companies resulted in the current Time Warner cable operations.[18]

Feb. 14, 1997); Adelphia Communications, Inc., 1996 10-Q (SEC filed Nov. 14, 1996); Adelphia Communications, Inc., 1995 10-K (SEC filed June 28, 1996); Adelphia Communications, Inc., 1995 10-Q (SEC filed Feb. 14, 1996); Adelphia Communications, Inc., 1994 10-Q (SEC filed Feb. 14, 1995); Adelphia Communications, Inc., 1994 10-Q (SEC filed Nov. 14, 1994); Adelphia Communications, Inc., 1994 10-K (SEC filed June 29, 1995); J. Flint, *Cabler Consolidation Current Craze*, Variety, at 43 (June 19, 1994); Comm. Daily at 11 (Mar. 2, 1990); Comm. Daily at 5 (Sept. 6, 1989); *Adelphia Communications Acquires Cable Systems in Virginia*, PR Newswire (Apr. 3, 1989); *Adelphia Communications Acquires*, PR Newswire (Mar. 24, 1988); Comm. Daily at 5 (Apr. 4, 1984); *Book Banned*, Associated Press State & Local Wire (Apr. 14, 1999); Advertising Age at 81 (Nov. 3, 1986); *Pennsylvania Company Buys FrontierVision*, Associated Press State & Local Wire (Feb. 26, 1999); Comm. Daily, Mass Media (Dec. 7, 1999); Electronic Media at 34 (Sept. 26, 1988); *Century Buys 3 Cable Units*, N.Y. Times, at D16 (July 6, 1988); *Century Communications Corp. Has Acquired Cowlitz Cablevision Inc.*, Bus. Wire (Nov. 18, 1986).

[17] *See* Rifkin Acquisition Partners, 1996 10-K (SEC filed Apr. 1, 1997); Comm. Daily at 9 (Oct. 21, 1986); *Target: Cable TV Systems Operations (Toledo, OH); Fanch Communications Inc.*, Mergerstat M&A Database (updated Jan. 15, 1998); Comm. Daily at 6 (Aug. 29, 1995); *Target: Outer Banks Cablevision; Falcon Cable Systems Co.*, Mergerstat M&A Database (updated Oct. 12, 1992); Avalon Cable, LLC, 10-Q (SEC filed Aug. 16, 1999); M. Farrell, *Smaller System Deals Close, Too*, Multichannel News, at 88 (July 12, 1999); *Local and State Actions*, Warren's Cable Regulation Monitor (Sept. 21, 1998); *Cable Notes*, Warren's Cable Regulation Monitor (June 8, 1998); *Target: Cross Country Cable Inc.; Avalon Cable Television*, Mergerstat M&A Database (updated Jan. 15, 1999); Renaissance Media Group LLC, 2000 10-K405 (SEC filed Mar. 30, 2001); American Cable TV Investors 5 Ltd., 2000 10-K405 (SEC filed Mar. 30, 2001); *Helicon Cable Communications Selects General Instrument to Provide Digital Systems and Consumer Set-Top Terminals for Its Cable Systems*, PR Newswire (Feb. 16, 1999); Comm. Daily (Apr. 14, 1998).

[18] Time Warner Inc., 1995 10-K (SEC filed Mar. 22, 1996); J.L. Sullivan, *The Cable Shakeout: OC Loses One HQ But Attracts New Investment*, Orange County Bus. J., at 1 (May 15, 1995); K. Maddox, *Time Warner Merges ATC, Warner Cable*, Electronic Media, at 3 (Aug. 17, 1992); *A Summary of Developments in the News Industry for the Week of Feb. 3-10*, Associated Press (Feb. 10, 1992); W. Belcher, *Leach Stops by to Mark Cable Deal*, Tampa Trib., at 4 (Apr. 19, 1996); *Broadcast TV*, Electronic Media, at 38 (July 10, 1989); *American Television and Communications Reports Second Quarter 1987 Financial Results*, Bus. Wire (July 15, 1987); K. Bulkley, *Denver's Paragon to Manage Rogers U.S. Cable TV Systems*, Denver Bus. J., at 9 (Oct. 10, 1988); *Business Briefs*, United Press Int'l (May 5, 1983); *ATC to Acquire Chapel Hill, N.C. Cable System*, Bus. Wire (Dec. 3, 1991); PR Newswire (Dec. 4, 1980); *Warner Cable Announces Expansion, Becomes Time Warner Communications*, Bus. Wire (Mar. 25, 1997); L. Aguilar, *Council Hears Complaints About Paragon Cable*, L.A. Times, at 10 (June 8, 1989); *In Brief*, Star Trib., at 3D (Aug. 2, 1994).

The result of all of these transactions is to reduce the number of major distribution outlets for video programming, and thereby to increase the likelihood of coordinated action among the ones that remain. Three years ago, the Commission recognized that, "[b]ecause cable operators generally do not compete against each other in their respective franchise areas, they may incur no loss from carrying the same programming networks and have little economic disincentive for coordinated action."[19] And, although the D.C. Circuit vacated the Commission's horizontal ownership limit in part because the record did not reflect "a serious risk of collusion," it did not dispute the "economic commonplace" that "collusion is less likely when there are more firms." *Time Warner*, 240 F.3d at 1130, 1132. Simply put, because there are now only a handful of firms that programmers can rely upon to reach enough viewers to sustain operations, the Commission must be particularly vigilant to ensure that those firms do not amass sufficient scale to diminish competition in the development of video programming.

The anticompetitive impact of the merger would be further exacerbated by the combined AT&T/Comcast's increased incentive and ability to discriminate in preference of its own programming. This discrimination will limit the viability of competing distributors – which cannot get access to prized programming – while limiting the audience of competing programmers – which cannot get carriage on the nation's largest video distributor.[20]

And there is, moreover, quite a lot of programming for AT&T/Comcast to favor. Both of these companies are significant content providers in their own right. As noted above, AT&T still owns a 25-percent interest in Time Warner Entertainment, which owns substantially all of the

[19] *AT&T/MediaOne Order*, 15 FCC Rcd at 9843, ¶ 56.

[20] *See AT&T/MediaOne Order*, 15 FCC Rcd at 9844, ¶ 58 ("Not only will the merged entity have attributable interests in a vast number of programming networks, including many of the networks with the largest number of subscribers nationwide, but new networks will reduce their chances for long-term success if they do not meet the terms and preferences of the merged firm.").

assets of HBO, Warner Bros., Time Warner Cable Networks, Cinemax, Comedy Central, Court TV, as well as many other popular film and entertainment companies. AT&T also owns an attributable interest in E! Entertainment, style., and iN DEMAND, as well as regional services such as Fox Sports New England, New England Cable News, and Pittsburgh Cable News Channel.[21] In addition, AT&T has an indirect ownership interest in Rainbow Media Sports Holdings, which includes national programs such as American Movie Classics, Bravo, Independent Film Channel, and Women's Entertainment, and regional program services such as the Fox Sports Net services and MSG Network.[22]

For its part, Comcast owns a majority share of QVC (one of the top 20 programming services in the country), and significant shares of the Discovery Health Channel, E! Entertainment, The Golf Channel, and others.[23] Comcast is also a substantial provider of regional content to Pennsylvania, Delaware, New Jersey, Maryland, North Carolina, Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, South Carolina, and Tennessee.[24]

This local programming – and especially the sports programming – is of great importance in the MVPD market. *See* Gertner Decl. ¶¶ 43, 45. According to RCN, "40-58% of cable subscribers would be less likely to subscribe to cable service if it lacked local sports programming, and . . . an additional 12% said they were not sure."[25] Without access to local sports programming, RCN assumes it would achieve a penetration rate of about 15 percent of the

[21] Public Interest Statement at 25.

[22] *Id.* at 20 & n.27.

[23] *Id.* at 15.

[24] *Id.* at 14-15.

[25] Initial Comments of RCN Telecom Services, Inc. at 18, CS Docket No. 01-290 (FCC filed Dec. 3, 2001).

homes it passes in each market it builds out, assuming a loss, on average, of 49 percent of homes passed due to absence of local sports, and a 30-percent penetration rate of the remaining 51 percent.[26] According to RCN, this rate is "so low that no entrepreneur would be willing to risk the hundreds of millions of dollars required to overbuild an urban area with modern fiber optic plant."[27]

Significantly, Comcast has already shown an unwillingness to make this regional sports programming available to competing MVPDs. For example, in the Philadelphia area, Comcast has refused to license its regional sports network to competing DBS providers. *See* Gertner Decl. ¶ 43. And DBS subscription rates there are well below the national average. *Id.* ¶ 45. Thus, Comcast not only has the ability and incentive to disadvantage its competitors by restricting access to content, it has a demonstrated track record of doing so.

The merger will only make this situation worse, as the combined company will be able to leverage a far larger array of regional content over an expanded service area, reducing competition for one-third of the country. Indeed, the potential anticompetitive havoc that can be caused has not escaped the merging parties' senior management. AT&T CEO C. Michael Armstrong has stated that the merging parties intend to "develop new and 'leverage' existing programming content." He pointed specifically to, among other things, Comcast's regional sports networks.[28]

Raising Rivals' Costs. Against all of this, the Applicants point mainly to the existence of alternative video platforms – primarily DBS – as providing sufficient competition to keep them

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[26] *Id.* at 18 & n.43.

[27] *Id.* at 18.

[28] C. Michael Armstrong, Chairman and CEO, AT&T, Presentation to Salomon Smith Barney Conference (Jan. 7, 2002).

from abusing their market power.[29] But, even as things stand today, DBS is plainly insufficient to check the dominant cable operators. For the past six years, cable prices have been rising at three times the rate of inflation.[30] Those operators most likely to face head-to-head competition from satellite "charge higher, not lower prices."[31]

More fundamentally, the merger will makes things *worse*, by diminishing the already strained ability of DBS and other platforms to compete. AT&T/Comcast's increased bargaining leverage stemming from the merger would not only diminish the amount and diversity of video programming, it also would increase the costs of rival distribution networks, both in- and out-of-region. As the attached declaration of Dr. Robert Gertner explains, the combined company's leverage will allow it to drive down the prices it pays for programming. *See* Gertner Decl. ¶¶ 24, 39-41. This is, in fact, what several studies have found: large MVPDs obtain significant discounts from cable networks.[32] And AT&T and Comcast themselves predict that they will achieve annual programming cost savings of $250 to $450 million.[33]

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[29] *See* Public Interest Statement at 66-67.

[30] *See* Mark Cooper, Consumer Federation of America, *The Failure of "Intermodal" Competition in Cable Markets* at 15 (Apr. 23, 2002) ("*CFA Study*"), *at* http://www.consumerfed.org/Intercomp.20020423.pdf; *see also* Report on Cable Industry Prices, *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992; Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment*, MM Docket No. 92-266, FCC 02-107, ¶ 22 (rel. Apr. 4, 2002) ("The cable [consumer price index ("CPI")] increased by 3.9% over the 12 months ending July 2001," outpacing the overall CPI's 2.7% increase.); *Comcast's Roberts Says AT&T Merger Will Benefit Consumers*, Comm. Daily, at 3 (Apr. 24, 2002) (noting that a "skeptical" Senator Kohl told Comcast President Brian Roberts that he was "doing an outstanding job in representing [his] company's best interest," but that "whether that is in the best interest of the consumers of America is open to debate").

[31] *CFA Study* at ii.

[32] *See* Gertner Decl. ¶ 39 (collecting sources).

[33] Pick Decl. ¶ 21 (Public Interest Statement App. 9).

Putting aside the question of whether a combined AT&T/Comcast would pass these discounts through to consumers, the fact remains that content providers – particularly those operating at a thin margin – will need to recoup the revenue elsewhere. To do so, they will seek greater revenues from other MVPD providers. Higher programming prices paid by other MVPDs may, in turn, reduce their incentives to upgrade their equipment. This could reduce the number of channels offered by other MVPDs. Higher programming costs may also imperil competing platforms – such as DBS – because they will be hard-pressed to gain any ground on the cable giants when the cable giants enjoy lower programming costs. *See* Gertner Decl. ¶¶ 23-26.

A combined AT&T/Comcast's ability to raise its rivals costs would be buttressed by the company's ownership of Headend in the Sky ("HITS"). HITS is a wholly owned subsidiary of AT&T Broadband that aggregates programming for MVPDs. HITS aggregates 150 digital programming channels from a variety of different satellites and delivers them in a single transmission path and in digitized format. This service allows MVPDs to reduce significantly their investment in head-end equipment; indeed, HITS can reduce a cable system operator's investment from $500,000 to about $30,000. Thus, HITS is a valuable service to overbuilders and others who want to provide video services.

Because AT&T/Comcast would own HITS, the combined company could refuse to offer its video programming services to any cable overbuilder that would compete with AT&T/Comcast anywhere in its vast geographic footprint. Indeed, based on HITS' past behavior, it appears that AT&T/Comcast would do exactly that. SBC recently inquired about obtaining video programming from WSNet, a firm that lists HITS as a strategic partner. WSNet "distribut[es] both digital and analog satellite television programming to the private cable and wireless cable industries serving the multiple dwelling unit (MDU) real estate sector" and serves "small and rural cable companies, and alternative access providers seeking a private label digital programming solution."[34] The bulk of WSNet's programming comes from HITS (although it contracts directly for some additional programming). SBC recently engaged in discussions with WSNet to see if WSNet could serve as a possible supplier for a Broadband Passive Optical Network ("BPON") application. But WSNet has informed SBC that HITS will not permit WSNet to sell HITS services to overbuilders – apparently defined as video distributors that cross a public right-of-way, and including the SBC BPON application in question – that compete with AT&T cable systems.

This conduct is transparently anticompetitive. And, with AT&T practically doubling the size of its geographic footprint, more of the same can be expected – but across a much wider territory. HITS programming would become unavailable to overbuilders not merely in the AT&T cable service areas, but in Comcast's as well.[35]

It is imperative that the Commission use the merger review process carefully to consider these potential harms. As noted at the outset, unlike in previous mergers,[36] the Commission does not have the luxury of simply asking whether the transaction would violate its existing horizontal ownership rule. Instead, it must carefully examine the likelihood that the merged company could foreclose access to programming, and take any steps necessary to ensure "the flow of video programming from the video programmer to the consumer."[37]

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[34] WSNet, *Frequently Asked Questions*, *at* www.wsnet.tv/FAQ/faq.asp#1.

[35] Comcast, too, has already demonstrated its desire to eliminate overbuilders. WideOpenWest, Comcast's only cable competitor in Michigan, recently alleged that "Comcast is trying to eliminate cable TV competition by giving customers who try to leave *unpublished* lower rates." *See* Brenda Rios, *Competitor Says Comcast Unfair*, Detroit Free Press (Apr. 2, 2002) (emphasis added).

[36] *See AT&T/MediaOne Order*, 15 FCC Rcd at 9844, ¶ 59.

[37] 47 U.S.C. § 533(f)(2)(A).

II. THE MERGER THREATENS COMPETITION IN THE MASS MARKET FOR BROADBAND SERVICES.

The impact of the merger on the broadband market would be equally severe. The facts regarding the cable industry's domination of the mass market for broadband Internet access are by now familiar. Cable has 69 percent of the broadband mass market,[38] and is adding new subscribers at a faster rate than competing high-speed technologies.[39] Indeed, not only are cable operators signing up new customers at a faster clip than incumbent LECs, they are *increasing* their already dominant market share.[40] And cable's existing dominance of broadband services appears likely to perpetuate. Analysts expect that cable will maintain a substantial lead over DSL at least through 2005.[41]

This merger threatens to cement the dominance of the cable platform over competing platforms. Even putting aside AT&T's interest in Time Warner, a combined AT&T/Comcast would control more than 23 percent of all residential broadband subscribers in the country and almost 34 percent of all cable modem customers.[42] After the merger, the top two cable

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[38] R.A. Bilotti, *et al.*, Morgan Stanley, Dean Witter, *Cable Modem and xDSL Conference Call* Exh. 3 (Jan. 18, 2002) (cable modem subscribers); xDSL.com, *TeleChoice 4Q01 DSL Deployment Summary* (DSL subscribers) *at* http://www.xdsl.com/content/resources/deployment_info.asp.

[39] *See, e.g.*, *UNE Fact Report 2002* at IV-19 to IV-20 & Figure 7 (Apr. 2002) (prepared for and submitted by BellSouth, SBC, Qwest, and Verizon in CC Docket No. 01-338, *et al.*).

[40] *See* R. Waters, *Baby Bells Hit By a Series of Wrong Numbers*, FT.com, at 2 (Apr. 16, 2002) ("[T]he Bells continue to lag behind the cable companies in the development of broadband services. . . . [T]heir high-speed DSL services have lost market share to cable modems."), *at* http://gloabalarchive.ft.com/globalarchive/article.html?id=020416000836.

[41] *See, e.g.*, N. Gupta, *et al.*, Salomon Smith Barney, *The Battle for the High-Speed Data Subscriber: Cable vs. DSL*, at 1 (Aug. 20, 2001) (cable will account for 59 percent of subscribers and DSL will account for 34 percent in 2005).

[42] R.A. Bilotti, *et al.*, Morgan Stanley, Dean Witter, *Cable Modem and xDSL Conference Call* Exh. 3 (Jan. 18, 2002); xDSL.com, *TeleChoice 4Q01 DSL Deployment Summary*, *at* http://www.xdsl.com/content/resources/deployment_info.aspl; J. Morris, *Satellite Internet*

companies – AT&T/Comcast and Time Warner – would control nearly 40 percent of residential broadband customers and almost 58 percent of all cable modem customers. The merger thus makes the major cable players both more important and less numerous, while minimizing the competitive significance of smaller players in the purchase of programming and content. And, as in the video market, size is not all. Because a combined AT&T/Comcast would have substantial interests in Internet content – and the ISPs and portals they use to access it – the merger substantially increases the parties' incentive and ability to discriminate in favor of affiliated content. As one analyst put it, "[t]o the benefit of its shareholders – but to the detriment of . . . vendors in the cable and communications industries – AT&T Comcast would be a powerful gatekeeper on a scale unrealized since the late 1980s."[43]

Horizontal Concentration and Vertical Foreclosure. The merger thus poses threats to the broadband mass market similar to those in the MVPD market, and perhaps even more so. The broadband market is nascent, and crucial new products and technologies are being developed quickly. Accordingly, as the Commission has previously recognized, any harm to this market at this critical stage will have long-lasting effects on consumer welfare.[44]

Indeed, as Dr. Gertner explains, compared to video programming, the broadband market is undeveloped, with far fewer total subscribers available to purchase content. Programmers may therefore have more difficulty securing the distribution and promotion necessary to justify

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Providers Facing Road Against Cable, DSL Competitors, Aerospace Daily, at 1 (June 13, 2001).

[43] George Mannes, *Telephone Temptress Reels in Comcast*, TheStreet.com, *at* http://www.thestreet.com/_ cnet/tech/georgemannes/10005703.html.

[44] Memorandum Opinion and Order, *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc. to AOL Time Warner Inc.*, 16 FCC Rcd 6547, 6599, ¶ 121 (2001) ("*AOL/Time Warner Order*") (acknowledging as a "public interest harm" the possibility that AOLTime Warner might "withdraw support from DSL – even if it were limited to Time Warner cable service areas, and even if its ultimate effect were only to *slow* DSL's continued growth") (emphasis added).

developing content, and may accordingly be more beholden to AT&T/Comcast's increased bargaining leverage. *See* Gertner Decl. ¶¶ 15, 17. As a consequence of this leverage, content providers may be forced either to reduce the quality or quantity of their content (because they lack funds sufficient to develop higher-quality or more programming) or to obtain greater revenues from cable modem competitors, such as DSL. In the first case, output is restricted and consumers and the public interest suffer. In the second case, the costs of rival distribution platforms are raised in an anticompetitive manner, with the same end result.

Coupled with their demonstrated proclivity to discriminate in favor of their own Internet content, moreover, the Applicants' presence in the ISP/portal market creates further cause for concern. "[U]nlike high-speed access offered over the telephone network where the customer can select the Internet Service Provider ("ISP") of his own choice, the cable ISP is selected by the cable provider and offered to customers in that cable operator's individual regions."[45] As the Commission has recognized, notwithstanding a smattering of recent transactions, cable operators typically offer only one ISP to customers.[46] As a general matter, that ISP is usually either owned by or affiliated with the cable operator. Thus, for example, Excite@Home previously had a contractual arrangement to be the exclusive portal on both AT&T's and Comcast's cable Internet service. Now Comcast has "transferred all of its high-speed Internet customers to a network that is owned and managed by Comcast."[47] AT&T has likewise provisioned a replacement network to provide Internet service to its customers.[48]

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[45] *Eighth Annual Video Report*, 17 FCC Rcd at 1266-67, ¶ 46.

[46] *Id.* at 1267, ¶ 46.

[47] Public Interest Statement at 12.

[48] *Id.* at 23.

The Commission thus need not speculate about whether a combined AT&T/Comcast might favor its own affiliated content to the exclusion of competing content. Both companies have a demonstrated history of doing so. Moreover, the merger would substantially aggregate interests in vertical markets, thus increasing the merging companies' ability and incentive to favor their affiliated content as well as that tailored to the cable platform. The result, of course, would be to disadvantage unaffiliated content providers – as well as competing platforms that rely on those unaffiliated content providers – to the detriment of consumers. And, as we now discuss, with the leading competitors hobbled by onerous regulation, the competitive pressure brought to bear on a combined AT&T/Comcast would likely be insufficient to force it to change its practices. *See* Gertner Decl. ¶¶ 17, 62.

Regulatory Obstacles to Competition. In the face of these potential harms, the Applicants contend that competition from competing broadband platforms – in particular, from DSL – will keep them in check.[49] To be sure, it was precisely the existence of such competition that mitigated the Commission's broadband-related concerns in AT&T's last major cable transaction.[50] But, whatever the merits of that view three years ago, in today's unbalanced regulatory environment, it cannot justify this transaction.

Indeed, this unbalanced environment is a major reason for cable's market dominance in the first place. SBC fully supports the Commission's recent steps toward a rational and balanced broadband regulatory framework. But those steps have yet to provide any actual regulatory

[49] Public Interest Statement at 92.

[50] *See AT&T/MediaOne Order*, 15 FCC Rcd at 9867, ¶ 117 ("there is evidence that ILECs, CLECs, and other competitive providers are aggressively rolling out alternative broadband technologies, notwithstanding cable's early lead in the nascent broadband area"); *id.* at 9867-68, ¶ 117 (premising approval in part on understanding that "DSL sales [we]re . . . growing at a more rapid rate than cable modem sales," and speculating that the recently promulgated line-sharing rules would "further spur the deployment of DSL broadband services").

relief, and the fact remains that DSL provided by incumbent LECs remains mired in comprehensive, burdensome, and costly regulation that is not imposed on cable operators. The upshot of this regulatory imbalance is to create a playing field that is severely tilted toward the dominant cable providers. Thus, telephone companies have to invest hundreds of millions of dollars to "unbundle" the wireline spectrum that they use for broadband, for example, and make it available to all comers at regulated prices. Cable companies, by contrast, do not bear these obligations or costs. Telephone companies must invest additional hundreds of millions of dollars to permit their competitors to "collocate" equipment in telephone company premises to make it easier to use that "unbundled" spectrum. Again, cable companies do not bear these obligations or costs. Telephone companies are almost completely locked out of the multi-billion dollar (and rapidly expanding) Internet backbone service. Cable companies are not. Telephone companies must offer their retail broadband transmission services to competitors at a federally mandated discount. Cable companies do not. Telephone companies have to contribute to universal service when they provide broadband access, bearing what is, in effect, a 7-percent tax on their service. Cable companies do not. Telephone companies have been forced to carve-out their broadband transmission services into a separate affiliate as a condition to gaining regulatory approval of recent mergers. Cable companies have not. And, perhaps most critically, telephone companies labor under the constant threat of additional regulations imposed by state commissions, which, in the absence of rules promulgated by this Commission, have turned their sights on ILEC broadband facilities. Cable companies, particularly now that the Commission has inoculated them from state regulation by classifying them solely under Title I,[51] face no such threat.

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[51] *See* Declaratory Ruling and Notice of Proposed Rulemaking, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities*, GN Docket No. 00-185 & CS Docket No. 02-52, FCC 02-77 (rel. Mar. 15, 2002) ("*Cable Classification Order*").

Any one of these impediments is enough to hinder the development of DSL. In the aggregate, their impact is staggering. And it is for precisely this reason that DSL has failed to emerge as a counterbalance to the dominant cable providers. To be sure, there are other disadvantages that telephone companies face vis-à-vis cable operators. In particular, whereas all cable plant is upgradeable, a significant portion of telephone plant is not. DSL service can be provided at high speeds only on loops that are 18,000 feet or shorter,[52] which means that "only about two-thirds of U.S. homes are easily addressable for xDSL."[53] Even when it is possible to upgrade the telco plant for DSL, cable still has an edge because cable has significantly lower upgrade costs than DSL.[54] As a result of these advantages, cable modem service is currently available to significantly more homes than DSL: cable modem service is already available to between 66 and 77 percent of U.S. households,[55] compared to only about 45 percent for DSL.[56]

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[52] *See, e.g.*, A. Gilroy & L. Kruger, *Broadband Internet Access: Background and Issues*, Congressional Research Service – Policy Papers (May 18, 2001); D. Sweeney, *Ultra Long-Reach DSL: A Whole New Crop of Companies Aims To Boost DSL Performance*, America's Network (Sept. 15, 2001).

[53] McKinsey & Co. and JP Morgan H&Q, *Broadband 2001* at 40 (Apr. 2, 2001) ("*Broadband 2001*").

[54] *See, e.g.*, *id.* at 69 ("xDSL starts life at a much higher cost point (close to $800) than cable modem (about $470) primarily because cable makes use of shared head-end terminating equipment, whereas DSL requires dedicated line cards for each subscriber.").

[55] *See* M. Goodman, Yankee Group, *Residential Broadband: Cable Modems and DSL Reach Critical Mass*, Media & Entertainment Strategies, Vol. 5, No. 3, Exh. 4 (Mar. 2001) ("*Yankee Group Critical Mass Report*"); *Broadband 2001* Tables 1 & 6. *See also* NCTA, *Industry Overview; Industry Statistics* (as of November 2001, 70 million households were passed by cable modem service), *at* http://www.ncta.com/industry_overview/indStat.cfm?ind OverviewID=2. The cable industry association estimates that, by year-end 2002, approximately 95 million U.S. homes (or nearly 90 percent of homes passed by cable) will have access to cable modem service. *See* NCTA, *Cable & Telecommunications Industry Overview 2001* Chart 2 (2001) (citing Morgan Stanley Dean Witter, *Broadband Cable Second-Quarter Review* at 9 (Aug. 29, 2001)).

[56] *See, e.g.*, *Yankee Group Critical Mass Report* Exh. 4 (estimating that DSL will be available to 45% of all households by year-end 2001); *See* J. Bazinet & D. Pinsker, JP Morgan

But, standing alone, these technical limitations would likely not have derailed DSL's efforts to compete with cable. In fact, to counter them, SBC announced Project Pronto, a $6 billion initiative designed to overcome these limitations and bring DSL to 20 million consumers that otherwise were out of reach.[57] No sooner had SBC announced this initiative, however, than CLECs began to clamor for access to the new facilities. And, after reviewing those requests for nine months, the Commission granted many of them, and then issued an NPRM proposing a raft of new sharing obligations.[58] With that NPRM pending, the CLECs took their arguments to the states, which – with no jurisdiction over cable modem service, and therefore little ability to compel intermodal competition – opened a series of proceedings to further burden the deployment of DSL service. The economic case for the initiative – already tenuous in light of ample existing facilities-based competition – became more so. And, as a result, SBC was compelled to drastically scale back the deployment of Project Pronto facilities, and is rethinking the deployment of potential successor technologies – such as BPON – for fear that they too will be swept up in a mandatory sharing regime. As SBC Chairman and CEO Edward E. Whitacre, Jr. has explained: "Today's regulatory rules and uncertainty artificially increase costs, affect how we invest capital and how we market our products and services. . . . No responsible company could justify fully deploying broadband capabilities and investing in new advanced networks in the face of this uncertain environment."[59]

H&Q, *The Cable Industry* Figures 12 & 36 (Nov. 2, 2001) ("*JP Morgan Cable Industry Report*") (DSL available to 43% of U.S. homes as of 1Q2001); P. Roche, *DSL Will Win Where It Matters*, McKinsey Quarterly 2001, No. 1 (2001) ("40 percent of all phone lines are ready for DSL").

[57] Second Memorandum Opinion and Order, *Ameritech Corp. and SBC Communications Inc.*, 15 FCC Rcd 17521 (2000).

[58] Third Further Notice of Proposed Rulemaking in CC Docket No. 98-147, Sixth Further Notice of Proposed Rulemaking in CC Docket No. 96-98, *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, 16 FCC Rcd 2101 (2001).

[59] *See SBC Reports Third-Quarter Results*, Investor Briefing, at 1 (Oct. 22, 2001), *at*

It is accordingly clear that, in today's uncertain regulatory environment, incumbent LECs face tremendous disincentives to deploy broadband facilities. Thus, unlike in AT&T's last major cable transaction, the Commission can have no confidence that DSL will emerge as a sufficiently strong counterbalance to offset the broadband market power that the Applicants would accrue as a result of this merger – at least not unless (and until) the Commission removes the regulatory obstacles to DSL deployment.

Standards and the Role of Microsoft. Another significant threat to competition and the public interest is the threat that a combined AT&T/Comcast could use its might to tilt standards away from competing broadband platforms such as DSL. *See* Gertner Decl. ¶¶ 59-60. Analysts recognize that the combined company will have "the dominant seat at the table in influencing technology standards."[60] The merged company will be able to use this seat to dictate standards and software for set-top boxes, which are critical to the development of interactive television. A combined AT&T/Comcast could also influence the development of sophisticated hardware and software needed to make caching work and to manage caching services. Caching is a key aspect of broadband service, as it improves the accessibility and delivery of popular, on-demand media clips and mitigates the large traffic spikes caused when many users access a particular source at one time (for example, to receive information on a breaking news event or to get a first look at popular new content). Absent adequate safeguards, the standards surrounding these services may favor the cable modem platform, and thereby further tilt the market away from DSL.

In this regard, it is no coincidence that Microsoft is involved in this transaction. Microsoft has spent many years (and billions of dollars) attempting to achieve a lasting presence

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http://www.sbc.com/Investor/Financial/Earning_Info/docs/3Q01_IB_Final.pdf.

[60] N. Gupta, Salomon Smith Barney, Equity Research: United States, Comcast Corporation, at 3 (Jan. 4, 2002).

in set-top boxes. As set-top boxes have been equipped with digital technology, they have hard drive and operating system capabilities.[61] Set-top boxes are therefore a key gateway into people's homes, for TV, broadband Web access, and Internet telephony. By the middle of 2000, more than 50 million set-top boxes were deployed in homes across North America, and there were perhaps twice that worldwide.[62]

Microsoft recognizes that "[t]he mainstream receiver platform for TVs is, without a doubt, the set-top box."[63] And it has sought to dominate the software market for set-top boxes just as it attempted to corner the browser market: "If everything goes as we hope, the majority of those set-top boxes will be running Microsoft TV instead of some competing piece of software."[64] Thus, Microsoft will control a "leading future challenger to the Windows monopoly."[65]

The pillar of Microsoft's strategy is to invest in cable companies, with the intention of selling them Microsoft set-top box software and establishing the industry standard. Between 1996 and 1999, Microsoft invested in 15 to 20 cable television companies.[66] It invested $212 million in Time Warner, and $1 billion in Comcast. And, in May 1999, Microsoft made an

[61] *Gates' Grand Internet Plan*, Bus. Rev. Weekly (Australia) (Sept. 15, 2000).

[62] Dominic Gates, *Gates and Malone Explore Cable Hookups*, Industry Standard (July 31, 2000).

[63] Jim Barthold, *Microsoft Whistling the Same Old Tune*, Cable World, at 60 (Sept. 11, 2000) (quoting Ed Graczyk, then-Director of Marketing Communications for the Microsoft TV Platform Group).

[64] *Id.*

[65] Amy Harmon, *Executive Fearful of Microsoft in Interactive TV Software*, N.Y. Times, at C2 (Apr. 3, 2002).

[66] Patrick Seitz, *Who Benefits, Who Loses Out in the Big Split – Proposed Microsoft Breakup Could Help Sun Microsystems, IBM, Oracle, But U.S. Firms May Pay More for Software*, Investor's Bus. Daily, at A4 (June 9, 2000).

investment five times larger than any direct U.S. cable company investment it had made previously: it staked $5 billion on AT&T Broadband.[67]

Microsoft plainly intends these investments in the leading cable companies to enable it to control set-top box software. In an internal email, Microsoft Chairman and CEO Bill Gates pointedly explained his understanding that Microsoft

> had convinced Comcast, AT&T and others to make it clear that all Cablelabs should do is OS [operating system] interop. I was very involved in this and I am stunned if this is going the other way without my hearing about it. This would be a total disaster for us in terms of our TV Platform efforts. We have to get the basics right and not allowing standards to destroy our position has got to be part of that.[68]

This merger makes it that much more likely that Microsoft would "get the basics right." It would give Microsoft a concentrated investment in the combined AT&T/Comcast that assuredly would enable it to "convinc[e]" the merged company – if any more convincing is necessary – to ensure that standards favor Microsoft's interests. And, because the merger greatly increases concentration in the cable industry, it makes it that much easier for Microsoft – with its hefty investments in AT&T/Comcast and number two Time Warner – to dictate the terms on which set-top boxes will operate.

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[67] *See* Jay Greene, *et al.*, *For Microsoft, It's "Inactive TV,"* Bus. Week, at 46 (Sept. 4, 2000). Microsoft's worldwide cable holdings are similarly vast. It invested $400 million in Canada's Rogers Communications. In Europe, Microsoft's stake in Britain's Telewest cost $3 billion, and it put more than $400 million into Netherlands-based UPC. It also invested $500 million in Telewest rival NTL, which afterward bought the cable division of Cable & Wireless to become the U.K.'s largest cable operation. In Latin America, Microsoft paid $126 million for 11 percent of Globo Cabo, a Brazilian cable company; and it invested $40 million in TV Cabo of Portugal. Dominic Gates, *Gates and Malone Explore Cable Hookups*, Industry Standard (July 31, 2000). Microsoft also owns 60 percent of the Japanese cable company Titus, now owned and merged with Japanese cable company Jupiter. Post-merger, the two U.S. companies thus jointly control the largest cable operator in Japan, offering broadband services in one of the most technologically advanced markets. *Id.*

[68] Plaintiffs' Exh. 334, *United States v. Microsoft Corp.*, Nos. 98-1232 & 98-1233 (D.D.C.) (E-mail from Bill Gates to Jon DeVaan and Craig Mundie (Aug. 18, 2000)).

Critically, the cable consortium – with AT&T/Comcast and Time Warner leading the way – can collaborate with Microsoft to use set-top box operating software to advantage cable operators at the expense of DSL. In exchange for exclusive contracts with cable companies to distribute its own set-top box software, Microsoft could put into its software triggers to activate certain features and functions that could only be used with cable-provided content, and therefore would be unavailable to DSL users. Thus, interactive links to information about video programming and other interactive television devices could be made available only with cable-provided content. With the popularity of interactive television on the rise, this would give cable a substantial advantage over DSL.

A merged AT&T/Comcast and Microsoft could collaborate in other ways to disadvantage competition. For instance, Microsoft could leverage its dominance of PC software and operating systems to steer new PC purchasers or set-top box users to cable modem, as opposed to DSL service. For example, Microsoft could insert a screen during the installation process for a new computer or set-top box that could ask consumers if they wish to obtain broadband service via their cable system and even to subscribe to MSN or the cable system's "home brand" ISP/portal service. Microsoft may also seek to leverage its operating software monopoly and ISP/portal position into other services, such as a comprehensive messaging service or a combined email and voicemail access service in order to obtain a return on its billions of dollars invested in AT&T/Comcast.

Or, to take another example, Microsoft and cable operators could work together to cache Microsoft and other favored content at major cable head-ends, which would improve the experience a cable modem customer receives when interacting with that content. *See* Gertner Decl. ¶ 59. Absent appropriate safeguards – in particular, open specifications facilitating the manufacture and sale of set-top boxes that have access to all of the same AT&T/Comcast

broadcast programming options, but are able to present their own electronic program guides, interactive programming links, and electronic commerce and content offerings – the companies might also seek to create a "walled garden" product that drives all content and electronic commerce requests to Microsoft.

Cable companies and Microsoft might also work with set-top box hardware makers to limit DSL's ability to use set-top boxes at all. Cable modem service has an inherent advantage over DSL in that the integration of video and broadband services is readily done over the cable network. One way DSL can minimize this disadvantage is to offer DSL service through an integrated set-top box that allows the provision of both DSL and video service. But those boxes are less likely to get developed if the cable companies persuade the leading manufacturers not to produce DSL-compatible boxes, in exchange for the cable companies' business. This is easily accomplished given the links between set-top box hardware makers and the cable companies. AT&T is a leading purchaser of Motorola set-top boxes, and AOL Time Warner is aligned with Scientific-Atlanta. If a combined AT&T/Comcast commits to discriminating against competing broadband platforms in the same manner as it has against competing video platforms, *see infra* pp. 11-14, there can be little doubt that, absent Commission intervention, it will seek to make set-top boxes incompatible with DSL.

III. VAGUE PROMISES OF VOICE COMPETITION CANNOT OFFSET THE PUBLIC INTEREST HARMS CREATED BY THE MERGER.

Commission precedent firmly establishes that the merger may be approved only if AT&T and Comcast demonstrate that the transaction will result in public-interest benefits that outweigh the competitive harms. These benefits must be "achievable only as a result of the merger," "sufficiently likely and verifiable," and "not deemed the result of anti-competitive reductions in output or increases in price."[69] Moreover, in view of the extensive competitive threat that the

[69] *SBC/Ameritech Order*, 14 FCC Rcd at 14825, ¶ 255.

merger poses in video distribution and broadband services, AT&T and Comcast are tasked with "demonstrat[ing]" benefits with "a higher degree of magnitude and likelihood than [the Commission] would otherwise demand."[70]

The Applicants' primary claim is that, whatever the harm the merger will cause to video and broadband services, it should be approved because it will purportedly "further . . . the deployment of facilities-based local telephone competition." Public Interest Statement at 36. If this contention has a familiar ring, it is because it is the exact same claim AT&T made to justify its two previous cable mergers. Thus, when AT&T sought Commission approval of its merger with MediaOne, it pledged that the combined company would "enhance competition for residential local exchange and exchange access services by enhancing the ability of AT&T and MediaOne to provide facilities-based local telephone service to mass market customers."[71] Likewise, AT&T previously claimed that its proposed union with TCI would enable it to "provide facilities-based residential service" by using TCI's cable facilities to provide for two-way voice telephony.[72]

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[70] *Id.* ¶ 256.

[71] AT&T/MediaOne Applications and Public Interest Statement at 33, CS Docket No. 99-251 (FCC filed July 7, 1999) ("*AT&T/MediaOne Public Interest Statement*").

[72] AT&T/TCI Description of Transaction, Public Interest Showing, and Related Demonstrations at 20, CS Docket No. 98-178 (FCC filed Aug. 31, 1998) ("*AT&T/TCI Public Interest Statement*"). Indeed, AT&T submitted "detailed deployment schedules to the Commission outlining its plans to deliver local exchange and exchange access services following the consummation of the merger." Memorandum Opinion and Order, *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc. to AT&T Corp.*, 14 FCC Rcd 3160, 3231, ¶ 148 (1999) ("*AT&T/TCI Order*"). There is no record of whether AT&T met those schedules. AT&T also resorted to the claim of local competition in attempting to justify its merger with Teleport, and the Commission relied on it in there as well. *See* Application for Authority to Transfer Control at 8, CC Docket No. 98-24, File No. I-T-C-98-104-TC (FCC filed Feb. 3, 1998) ("In the near term, AT&T expects that the acquisition of TCG will accelerate and expand AT&T's provision of facilities-based local exchange service, primarily to business customers and to multiple dwelling units in high density markets currently served by TCG."); Memorandum Opinion and Order, *Teleport*

There is, however, a distinct difference between the rationale AT&T offered then, and the one it offers now. In both the TCI and MediaOne transactions, AT&T claimed that its proven abilities *as a telephone company* would allow it successfully to deploy cable telephony to the mass market.[73] In fact, it was precisely this synergy that caused the Commission to view those transactions as serving the public interest.[74] Here, however, the merging parties appear to believe that jettisoning those traditional telephone company assets – and returning AT&T's cable assets to a "pure" cable company – is necessary to fulfill the promise of cable telephony. The Applicants cannot have it both ways. In light of this turnaround, the Commission should be highly skeptical of AT&T's pledge here.

Such skepticism is all the more warranted in light of Comcast's oft-stated reluctance to embrace cable telephony. Until this merger, Comcast had made unmistakably clear that it viewed circuit-switched cable telephony with disdain, and that it would only offer telephony "'if there is a way to deliver it with IP.'"[75] Having thus taken "'a hard look at the phone business'"

Communications Group, Inc. and AT&T Corp. For Consent to Transfer of Control of Corporations Holding Point-to-Point Microwave Licenses and Authorizations to Provide International Facilities-Based and Resold Communications Services, 13 FCC Rcd 15236, 15262-63, ¶ 50 (1998) ("in their applications, Applicants have explicitly identified a set of residential customers that will be served immediately, and thereafter, by the merged entity – customers that live in multiple dwelling units in high density markets") (internal quotation marks omitted).

[73] *See AT&T/MediaOne Public Interest Statement* at 22 (merger would purportedly enhance local voice competition by "combining existing cable facilities with AT&T's strong telephony brand, sophisticated knowledge of marketing telephony services, and technical expertise in establishing and managing telephone networks"); *AT&T/TCI Public Interest Statement* at 19-20 ("AT&T contributes its experience in providing toll-quality voice and data traffic, switching technology, a brand name that can compete with incumbent local telephone companies and capital").

[74] *See AT&T/MediaOne Order*, 15 FCC Rcd at 9820, ¶ 7; *AT&T/TCI Order*, 14 FCC Rcd at 3228-31, ¶¶ 145-148.

[75] Michael Lafferty, *Cable Telephony Sending Mixed Signals*, Communications Eng'g & Design (Apr. 2001) (quoting Mark Coblitz, Comcast vice president of strategic planning), *at* http://www.cedmagazine.com/ced/2001/0401/04a.htm.

and "examining the amount of capital required," Comcast previously concluded that it is "too expensive . . . given that cheaper Internet-protocol telephony solutions could arrive in two to three years."[76] Even now, Comcast's own Senior Vice President for Corporate Development candidly admits that "[t]o date, Comcast's experience with cable telephony has been relatively limited," and that "Comcast has not yet developed any new cable telephony networks on its own initiative, nor has Comcast developed the experience or infrastructure to expand cable telephony on its own."[77]

Indeed, careful examination of the Applicants' claims regarding local competition reveal just how limited they really are. Comcast has committed to offer cable telephony in only two markets, Detroit and Philadelphia,[78] where "AT&T has *already* invested" in the necessary "switching infrastructure."[79] That means that those markets can be served off AT&T's *existing* switches, with virtually no new investment. And, by all accounts, that is exactly what the parties intend to do. Its claims to this Commission notwithstanding, the truth is that Comcast is "'not touching circuit-switched telephony with a 10-foot pole.'"[80] It plans only to "'maintain what AT&T has done because . . . the expense has already been incurred.' That expense doesn't

[76] M. Stump, *Comcast's Phone Forecast: Legacy Subs in Black by '02*, Multichannel News, at 25 (Aug. 27, 2001) (quoting David Watson, Comcast executive vice president of sales, marketing and customer service).

[77] Pick Decl. ¶ 10 (Public Interest Statement App. 9).

[78] *See* Public Interest Statement at 38.

[79] M. Farrell, *AT&T Wants to Tweak Digital Packages Again*, Multichannel News, at 1 (Jan. 14, 2002) (emphasis added).

[80] Jim Barthold, *Comcast Pulls Telephony Turnaround*, Telephony (Jan. 7, 2002) (quoting Michael Goodman, Yankee Group).

include buying switches" or otherwise making any meaningful investment in facilities-based competition.[81]

It is accordingly clear that any increase in cable telephony deployment that the parties plan is not remotely merger-specific: a limited joint venture would easily permit AT&T to serve the customers in question off its own switches, without requiring a full scale merger. Thus, as we discuss in more detail below, if the Commission is to rely on the prospect of cable telephony to temper the threat that the merger poses in broadband and video services, the Commission must take steps to encourage the merged company to invest in *new* facilities to bring *new* services to *new* areas that would not otherwise be served. Absent such conditions, the Applicants' claims regarding local telephony are just so much talk, and nothing more.

IV. ABSENT SPECIFIC AND VERIFIABLE CONDITIONS, THE MERGER CANNOT BE APPROVED.

Like the Commission's current Chairman, SBC believes that any conditions imposed in the merger context should be closely tied to and "squarely supported by the analysis of the harms" of the merger.[82] In this context, that means imposing conditions aimed at (a) addressing the merged company's power over the MVPD market; (b) protecting the nascent broadband market from further dominance by the entrenched cable incumbents; and (c) encouraging the merged company to follow through on its commitment to provide facilities-based voice competition to residential customers.

MVPD Conditions. As noted above, the Applicants appear to concede that they must divest themselves completely of their interest in Time Warner Entertainment to gain approval of the transaction. But that is only a starting point. Even without an interest in Time Warner, the

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[81] *Id.* (same) (alteration in original).

[82] *SBC/Ameritech Order*, 14 FCC Rcd at 15214 (separate statement of then-Commissioner Powell).

merged company would possess significant power in the MVPD market. The Commission must take at least two additional steps to ensure that the Applicants do not abuse that power.

Program Access Rules. The 1992 Cable Act bars cable operators from using their control over programming to suppress alternative means of distribution.[83] The Act's program access regime prohibits cable operators from "unduly or improperly" influencing programming vendors in their dealings with unaffiliated distributors[84] or from discriminating against those competitors in the terms offered.[85] The Act and the Commission's implementing restrictions,[86] however, only apply to *satellite*-delivered programming.[87]

All video programming, including all the content distributed over conventional cable TV channels, is now moving toward digital format,[88] and once the content is digital, it can readily be distributed to cable head-ends via the Internet. Cable operators have already begun using fiber-optic delivery as an alternative. As they migrate their content to Web-based distribution, they can apparently escape their program-access obligations entirely. Indeed, that is precisely what

[83] 47 U.S.C. § 548; 47 C.F.R. § 76.1002.

[84] 47 U.S.C. § 548(c)(2)(A); 47 C.F.R. § 76.1002(a).

[85] 47 U.S.C. § 548(c)(2)(B); 47 C.F.R. § 76.1002(b). This prohibition applies to both price and non-price forms of discrimination, such as unreasonable refusals to deal. *See* Notice of Proposed Rulemaking, *Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992; Development of Competition and Diversity in Video Programming Distribution and Carriage*, 8 FCC Rcd 194, 198, ¶ 15 (1992).

[86] 47 C.F.R. §§ 76.1000-.1004.

[87] Memorandum Opinion and Order, *Echostar Communications Corp. v. Comcast Corp.*, 14 FCC Rcd 2089, 2099, ¶ 21 (1999).

[88] Digital formats are already easier to store, edit, and process; they will soon be easier and cheaper to create at the outset.

Comcast did when it decided to deny regional sports programming to competing distributors in the Philadelphia area. *See supra* p. 11.[89]

The Commission is "aware of the potential for this type of migration and the possible need to address it in the future."[90] The future is now. Regrettably, the concentration of increasing amounts of power among the top cable operators and their captive Internet portals and Web-based content providers could well signal the demise of cable's only serious competitor in MVPD, DBS. This merger is the continuation of a massive trend of "vertically integrated programmers beg[inning] to switch from satellite delivery to terrestrial delivery for the purpose of evading the Commission's rules," and the Commission must now impose "'an appropriate response to ensure continued access to programming.'"[91]

The Commission must accordingly condition its approval of the merger on AT&T/Comcast's agreement to distribute its programming on a nondiscriminatory basis regardless of the technology used to distribute its content at the wholesale level. This is particularly important with respect to the combined company's regional sports programming, which – as discussed above – Comcast has refused to make available to its video competitors.

Divestiture of HITS. The Commission must also insist upon complete divestiture of HITS to an unaffiliated third party. As explained above, HITS provides a critical service to

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[89] RCN has asked the Commission "to face up to the commercial reality that the cable industry is resorting to terrestrial transmission in large part to avoid the program access provisions of § 628 of the Act." Comments of RCN Corp. at 20-21, CS Docket No. 99-230 (FCC filed Aug. 6, 1999).

[90] *AT&T/TCI Order*, 14 FCC Rcd at 3180, ¶ 37.

[91] *Id.* ¶ 37 n.119 (quoting Memorandum Opinion and Order and Notice of Proposed Rulemaking, *Implementation of the Cable Television Consumer Protection and Competition Act of 1992*; *Petition for Rulemaking of Ameritech New Media, Inc. Regarding Development of Competition and Diversity in Video Programming Distribution and Carriage*, 12 FCC Rcd 22840, 22861, ¶ 50 (1997)).

start-up MVPDs, yet AT&T has already made clear that it will refuse to permit service to overbuilders in its territory. The only remedy for this blatantly discriminatory conduct is to force the merged company to divest itself of all interest in HITS as a condition precedent to consummation of the merger. The Commission should insist, moreover, that the acquiring party be financially sound, capable of successfully continuing the business, and completely unrelated to the merged company. Nor should the Commission permit any eventual buyback of the divested entity. Particularly in light of AT&T's history of anticompetitive conduct with respect to this service, only complete divestiture to an established concern will suffice to mitigate the threat posed by the merger.

Broadband Conditions. As discussed above, the merger poses a serious threat to the unfettered development of Internet content and to the viability of competing platforms – particularly DSL. By increasing the merging parties' already substantial leverage over content providers, the merger heightens the risk that the Applicants would foreclose competing content, set standards to favor the cable platform, and tilt the market further away from DSL.

By far the best resolution of these competitive concerns is to free ILECs to compete with cable on an equal footing. The Applicants themselves claim – and the Commission itself recognized in *AT&T/MediaOne* – that the DSL platform has the potential to provide a substantial competitive counterbalance to cable's increasing market share. But that can only happen if the Commission removes the burdensome and costly regulations that diminish ILECs' incentives aggressively to deploy broadband facilities. *See* Declaration of Dennis W. Carlton ¶¶ 8-11 (Attachment B hereto); Gertner Decl. ¶ 62.

The Commission has a number of open dockets in which it can do exactly that. In the *Information Services NPRM*, the Commission proposes to deregulate ILEC-provided broadband Internet access as a Title I information service, and to remove the underlying *Computer Inquiries* requirements that force BOCs to strip out a separate telecommunications component and offer it on a common carrier basis. In the *Triennial Review*, the Commission has before it an extensive record that demonstrates beyond legitimate dispute that CLECs are not "impaired" without access to the network elements that ILECs use to provide broadband services. And in the *Non-Dominance Proceeding*, the Commission properly proposes to remove all dominant-carrier regulation associated with ILEC broadband services.

The outcome of those proceedings will have a material effect on the competitive significance of this merger. If the Commission adheres to the goal of establishing a balanced, deregulatory framework for ILEC broadband,[92] then it can be reasonably confident that the ILECs will provide sufficient competition in broadband to diminish the threat posed by this merger. But the Commission cannot allow this merger to go forward as long as ILECs are incapacitated by regulations. To do so could irreparably damage the development of competition in broadband. Indeed, because broadband services are at such a critical stage – and because the

[92] *See, e.g.*, Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, CC Docket Nos. 02-33, 95-20 & 98-10, FCC 02-42, ¶¶ 4-6 (rel. Feb. 15, 2002) (articulating goals of "conceptualiz[ing] broadband broadly" across platforms, regulating broadband services "in a minimal regulatory environment," and "develop[ing] an analytical framework that is consistent . . . across multiple platforms"). *See generally*, *e.g.*, Michael K. Powell, Chairman, FCC, Remarks at the ITU Second Global Symposium for Regulators, Geneva, Switzerland (Dec. 4, 2001) (what is necessary is "a regulatory environment that provides the incentives necessary to deploy new services on the part of the private sector. The more onerous the regulatory environment, the costs of deployment become higher and riskier and more difficult."); *Cable Bureau Suggests Regulatory Forbearance for New Services*, Comm. Daily (Feb. 23, 2001) (noting Chairman Powell's comments that the Commission must move toward "some degree of less regulation" in the broadband market that would be "not so technology-centric"); Kevin J. Martin, Commissioner, FCC, *Framework for Broadband Deployment*, Remarks at the National Summit on Broadband Deployment (Oct. 26, 2001) (the current regime "creates significant disincentives for the deployment of new facilities that could be used to provide broadband. Under such a regime, new entrants have little incentive to build their own facilities, since they can use the incumbents' cheaper and more quickly. And incumbents have some disincentive to build new facilities, since they must share them with all their competitors.").

merger poses such a severe threat – the Commission cannot permit the merger to close unless and until it has actually cleared away the obstacles blocking competition from ILECs. Proposals alone are not enough. Absent effective rules creating deregulatory parity, the merger should not be allowed to proceed.

Accordingly, even if the Commission is confident that it will *eventually* free ILECs to compete with cable on an equal footing, it must take steps *now* that will protect competition until those rules take effect. The Commission's existing broadband dockets are unlikely to be concluded until much later this year, and even then they will surely be subject to a series of appeals that will create continued uncertainty.[93] If the Commission does not prevent the closing of the merger until these dockets are completed, then, in the interim – *i.e.*, until ILECs have sufficient certainty regarding their deregulatory status to deploy aggressively broadband facilities – the Commission must take affirmative steps to level the playing field. That means forcing the combined AT&T/Comcast to compete on terms and conditions that are comparable to those that apply to incumbent LECs:

Spectrum Unbundling. To provide true parity, the Commission must force the Applicants to unbundle spectrum and make it available at cost-based rates. Cable spectrum is already "unbundled" to some degree, of course – cable operators are required to set aside video channels for use by various third parties.[94] In terms of spectrum required, a cable modem service requires two channels: one channel for downstream traffic and another channel for upstream

[93] *Cf. Brand X Internet Servs. v. FCC*, No. 02-70518, *et al.* (9th Cir. filed Mar. 25, 2002) (challenging FCC's *Cable Classification Order*).

[94] *See, e.g.*, 47 U.S.C. § 532(b)(1) ("A cable operator shall designate channel capacity for commercial use by persons unaffiliated with the operator . . . ."); *see also id.* § 522(4) (a "channel" is "a portion of the electromagnetic frequency spectrum which is used in a cable system and which is capable of delivering a television channel"); *see generally FCC v. Midwest Video Corp.*, 440 U.S. 689 (1979).

signals, each consisting of approximately six MHz.[95] Upgraded cable systems – *i.e.*, those that are capable of providing cable Internet service – typically have a bandwidth of between 550 and 750 MHz, approximately ten percent of which is unused.[96] Any claim that hybrid fiber-coax is too limited to support unbundling is accordingly indefensible (especially when placed side by side with the conclusion that spectrum unbundling makes perfect sense in the much narrower capacity of copper wires).

Nor may the Applicants duck this obligation on the grounds of technical infeasibility. Unbundling spectrum poses no significant risk to cable systems, much less a risk substantial enough to permit them to operate a closed system.[97] That certain incumbent cable operators already connect with unaffiliated ISPs, and provide data transmission capacity over hybrid fiber-coax to that ISP, is evidence that transmission capacity can be provided (and spectrum isolated) to unaffiliated providers without adversely affecting traditional cable services.[98] And, to the

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[95] *See Overview of Cable Modem Technology and Services*, Cable Datacom News ("To deliver data services over a cable network, one television channel (in the 50-750 MHz range) is typically allocated for downstream traffic . . . and another channel (in the 5-42 MHz band) is used to carry upstream signals."), *at* http://www.cabledatacomnews.com/cmic/cmic1.html.

[96] *See* Sanford C. Bernstein & Co. and McKinsey & Co., Inc., *Broadband!*, at 39 (Jan. 2000) ("approximately 90%" of upgraded cable capacity "is taken up by traditional video services," and cable operators have "tremendous flexibility to reallocate system bandwidth").

[97] *Cf.* Decision, *Use of the Carterfone Device in Message Toll Telephone Service*, 13 F.C.C.2d 420, 424 (1968); *see also Hush-A-Phone Corp. v. United States*, 238 F.2d 266, 269 (D.C. Cir. 1956) (a customer is free to use communications services in ways which are "privately beneficial without being publicly detrimental").

[98] *See* Third Report and Order in CC Docket No. 98-147, Fourth Report and Order in CC Docket No. 96-98, *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, 14 FCC Rcd 20912, 20943, ¶ 63 (1999) ("*Line Sharing Order*") (relying on the fact that ILECs "already provide both analog voice and high-speed data services over one loop by connecting the local loop facility to their DSLAM to utilize the loop's non-voiceband frequency data transmission capability for their own xDSL services"), *petitions for review pending*, *United States Telecom Ass'n v. FCC*, No. 00-1012, *et al.* (D.C. Cir. argued Mar. 7, 2002).

extent that allocation of data channels may cause the cable equivalent of intermodulation or guardband distortions, the Commission may simply force the Applicants, as it did for ILECs in its *Line Sharing Order*, to remedy such problems.[99]

Indeed, all of the technical infeasibility arguments were made to – and rejected by – the Commission in the context of ILEC spectrum unbundling. The Commission justified imposing spectrum unbundling on the grounds that it would lower entry barriers, increase competition, accelerate the roll-out of broadband services, and prevent ILECs from leveraging their dominant position in the local exchange market into adjacent content markets.[100] These economic rationales apply with even greater force to a dominant competitor than they do to a nondominant one.[101] As the above discussion makes clear, the Applicants have more power than ILECs – not less – to leverage control over cable plant into the adjacent ISP market. To prevent them from

[99] The FCC has raised the bar even higher: line sharing will not be considered technically infeasible unless the ILEC can demonstrate to the state commission that DSL conditioning "would interfere with the analog voice service of the line." *Id.* at 20952, ¶ 81. The Applicants, with wires more capacious than the copper pair, must be held to the same standard.

[100] *See id.* at 20916, ¶ 5 (lack of access "materially diminishes the ability of competitive LECs to provide certain types of advanced services to residential and small business users, delays broad facilities-based market entry, and materially limits the scope and quality of competitor service offerings"); *id.* at 20930, ¶ 35 ("we find that unbundled access to the high frequency portion of the loop offers the best opportunity to see these nascent markets evolve into competitive markets"); Third Report and Order and Fourth Further Notice of Proposed Rulemaking, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 15 FCC Rcd 3696, 3783, ¶ 190 (1999) ("*UNE Remand Order*") (without access to DSL-capable loops, ILECs, "rather than the marketplace, would dictate the pace of the deployment of advanced services"), *petitions for review pending, United States Telecom Ass'n v. FCC*, Nos. 00-1015 & 00-1025 (D.C. Cir. argued Mar. 7, 2002); Report and Order, *Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services*, 14 FCC Rcd 4289, 4295, ¶ 9 (1999) ("BOCs remain the dominant providers of local exchange and exchange access services in their in-region states, and thus continue to have the ability to engage in anticompetitive behavior against competitive ISPs.") (footnote omitted).

[101] *Line Sharing Order*, 14 FCC Rcd at 20929, ¶ 32 (noting necessity of considering actual market activity).

doing so while ILECs remain regulated, the Commission must force them to unbundle spectrum and permit competitors to differentiate, to some degree, the quality and features of their service offerings.

Advanced Services Affiliate. To ensure the efficacy of a spectrum unbundling requirement, the Commission should force the Applicants to carve out their own cable modem service operations into a separate subsidiary that would stand on equal footing with competing providers and interact with the cable incumbent through nondiscriminatory OSS interfaces. In recent ILEC mergers, the Commission required the merging parties to create separate advanced services affiliates that would "level [the] playing field between [the ILEC] and its advanced services competitors," and "greatly accelerate competition in the advanced services market by lowering the costs and risks of entry and reducing uncertainty, while prodding all carriers, including [the ILECs], to hasten deployment."[102] The same economic logic should require cable operators – with approximately 70 percent of residential broadband users, and tentacles into upstream and downstream markets – to place their advanced services in separate affiliates, and to comply with the Commission's affiliate transactions rules.[103]

It is important to note that SBC advances these conditions reluctantly. Unlike some other parties that frequently appear before the Commission – in particular, AT&T – SBC has always been principled in its position that *de*regulation across-the-board is the best possible approach to broadband services. Open competition among the various platforms – unfettered by costly and cumbersome regulation – is by far the best alternative for consumers, competitors, and their respective shareholders and employees. But this is not what we have in place today. Instead, we

[102] *SBC/Ameritech Order*, 14 FCC Rcd at 14859-60, ¶ 363; Memorandum Opinion and Order, *Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control*, 15 FCC Rcd 14032, 14149, ¶ 261 (2000).

[103] *See, e.g.*, 47 C.F.R. § 32.27.

have a truly upside-down state of affairs, where the dominant providers compete free from all regulation, while the second-to-market, nondominant players are stifled by burdensome regulation. As long as this perverse imbalance is in place, the Commission should not approve a transaction that will only contribute to the already decisive advantages that the dominant cable incumbents enjoy in the marketplace.

Open Access. The Commission should also impose an "open access" requirement equivalent to that imposed by the FTC and endorsed by this Commission in connection with the AOL Time Warner merger. As explained above, with few exceptions, cable operators in general – and the Applicants in particular – generally prevent unaffiliated ISPs and portals from accessing cable customers directly. This merger would make the anticompetitive consequences of that practice, by increasing the number of households that a single firm can foreclose. Access akin to that imposed on Time Warner cable systems could partially mitigate this concern, by helping to ensure that content providers are not foreclosed from reaching the Applicants' broadband subscribers.

The Commission should not be deceived by Comcast's eleventh-hour agreement to carry United Online, and AT&T's similarly last-ditch deals with Earthlink and NET1 Plus. These deals raises many of the same problems that tripped up AOL Time Warner's "voluntary" open access pledge. In particular, their lack of transparency renders it impossible to determine whether they involve "brand" restrictions, "non-discriminatory" terms of carriage, or "troubling . . . pricing conditions."[104] Absent some assurance that the terms of these deals reflect a fair accommodation of the competing interests – and are not simply another example of the Applicants' ability to exert leverage over content suppliers – the Commission should place no stock in them.

[104] *See AOL/Time Warner Order*, 16 FCC Rcd at 6589-90 ¶¶ 94-95.

Indeed, absent Commission intervention, there is every reason to believe that the Applicants will *not* provide meaningful access to unaffiliated ISPs. Years ago, AT&T told the Commission that it would negotiate "private contracts with *multiple* ISPs in order to offer those ISPs reasonably comparable access prices, the opportunity to market and bill consumers directly, and the opportunity to differentiate service offerings and to maintain brand recognition in all such offerings."[105] The Commission expressly relied on that promise in approving AT&T's last cable merger.[106] But AT&T still has not delivered. One confidential agreement with a *single* nationwide ISP – and another with a regional ISP with fewer than 15,000 residential customers[107] – hardly qualifies as access for "multiple" ISPs. Moreover, there is reason to believe that other access negotiations have broken down because AT&T *refuses* to allow competing content providers "to maintain brand recognition" in their offerings.[108] Thus, absent unfettered competition between DSL and cable modem service, Commission intervention is necessary to force the Applicants to provide meaningful access to ISPs, for they plainly will not do so on their own.

Local Competition Conditions. As noted above, to offset the competitive harms posed by the merger, the Applicants claim that their transaction is necessary to increase local voice competition. In truth, however, the Applicants promise to offer service only to existing customers that are *already* within reach of AT&T's switches, and that could *already* be served

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[105] *AT&T/MediaOne Order*, 15 FCC Rcd at 9870, ¶ 121 (emphasis added).

[106] *See id.* ("We expect the Applicants to adhere to the foregoing commitments . . . .").

[107] *See* AT&T Press Release, *AT&T Broadband and NET1 Plus Reach ISP Choice Agreement* (Apr. 23, 2002).

[108] *See* J. Angwin & M. Peers, *AOL Rethinks Its Game Plan on Internet Access*, Wall St. J., at A6 (Apr. 19, 2002) (noting that AOL's "[t]alks with most of the top 10 cable operators have stalled [in part] over the cable industry's demands" regarding "who 'controls' the customer").

through a simple joint marketing agreement. The Applicants have made no commitment to invest in new facilities, and apparently have no plans to do so.

Particularly in light of the significant competitive threat posed by the merger, the Commission should have every reason to expect more. Fully 77 percent of all homes in the United States are served by cable with two-way capabilities,[109] and cable operators already offer circuit-switched telephony services to 10 percent of all U.S. homes.[110] In those areas in which it is offered, consumers have responded. Of the 10 million homes in which cable telephony is offered, 1.5 million have subscribed – a healthy 15 percent penetration rate. Putting aside their apparent unwillingness to commit to providing voice service, the Applicants plainly have no technical justification – and little business justification – for refusing to deploy telephony throughout their region.

None of this is to say, however, that SBC believes that the Commission should mandate specific deployment targets, as it did in the *SBC/Ameritech Order*. SBC continues to believe that the Commission should refrain from interfering in a company's decisions whether to enter a particular geographic area, or to offer a particular service. As Chairman Powell has explained, such interference risks "substitut[ing] regulators' judgments about how communications resources should be allocated for the judgments of consumers and competitors in the marketplace."[111]

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[109] *Broadband 2001* Table 6.

[110] *JP Morgan Cable Industry Report* at 53 & Table 22; NCTA, *Cable Telephony: Offering Consumers Competitive Choice* at 2 (July 2001).

[111] Memorandum Opinion and Order, *Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control*, 13 FCC Rcd 18025, 18171 (1998) (separate statement of then-Commissioner Powell).

Instead, the Commission should take steps simply to encourage the Applicants to deploy cable telephony more broadly. In this regard, perhaps the chief obstacle to true facilities-based competition in the residential segment has been, and remains, the availability of the UNE-platform. The platform is, of course, "physically similar to resale. In each case, the CLEC uses the ILEC network to provide service to the end user and essentially limits its own functions to marketing, inputting the order into the ILEC's systems, and billing."[112] Accordingly, the UNE-P is defined not by expanding output, consumer choice, product quality, or market price, but by federal and state regulators and the TELRIC pricing regime. Because it has been easier and cheaper for CLECs to piggy-back on the incumbent's network permanently rather than build out networks of their own, CLECs have adopted business strategies that center on indefinite reliance on UNEs.[113] And, although the Commission hoped that competitors would rely on UNEs only until it is "practical and economically feasible to construct their own networks,"[114] the UNE-P has, in fact, become the end-game in the residential market.[115]

[112] Commerce Capital Markets, *Status and Implications of UNE-Platform in Regional Bell Markets* (Nov. 12, 2001).

[113] *See, e.g.*, *UNE Fact Report 2002* at II-18 to II-19; Ex Parte Letter from Albert H. Kramer, Dickstein Shapiro Morin & Oshinsky (representing Birch Telecom) to Dorothy Attwood, Chief-CCB, FCC, CC Docket No. 96-98, at 1 (filed Jan. 17, 2001) ("it is not economical to self-provision switching for customers served by individual analog lines, even where a switch has already been deployed and the cost of that switch is regarded as a sunk cost") (emphasis omitted); *id.* at 3, 7 (Birch has "abandon[ed] serving customers using self-provisioned switching, unless those customers have sufficient needs to justify a DS-1 facility" and will not even serve customers that are "located a few blocks from one of its switches," despite the fact that "Birch has been able to rapidly build a customer base").

[114] *UNE Remand Order*, 15 FCC Rcd at 3701, ¶ 6.

[115] Thus, for example, AT&T continues to free-ride on ILEC facilities, with no end in sight. AT&T provides UNE-P service to approximately one million residential customers in New York and approximately 400,000 in Texas – enough customers, in New York alone, to fill five to ten switches. AT&T also operates 19 local voice switches in New York and 22 in Texas. Yet AT&T does not appear to have converted a single residential customer in New York or Texas to its own switch. The experience has been no different in other states where AT&T has

The platform has accordingly substantially diminished the incentives of CLECs – particularly cable providers – to invest in their own facilities. To ensure that it does not have that effect with respect to the merged company, the Commission should take the simple step of requiring the merged company to forego reliance on the UNE-P in any areas where it has cable facilities. If, as the Applicants claim, the merger will make the Applicants "better able to expand the availability of telephony over the Comcast systems more quickly, at less expense, and in a more customer-friendly manner" than has previously been available,[116] the condition will not impede competition. On the contrary, it will ensure that the combined company's self-proclaimed incentive to deploy facilities-based competition is not undermined by the prospect of regulatory arbitrage.

This condition should also extend to any company that engages in joint marketing arrangements with the merged company to sell the merged company's local exchange service. As AT&T itself has emphasized, customers are increasingly buying "a bundled package of local and long distance services,"[117] and it appears that is indeed how the Applicants plan to market their local service.[118] To ensure that the Applicants do not circumvent this condition merely by teaming with a carrier – say, for example, a long-distance carrier – that itself utilizes the platform

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signed up large numbers of UNE-P customers. *See UNE Fact Report 2002* at II-17 to II-18 & nn.54-55; *see also* Supplemental Declaration of Michael Lieberman ¶ 20, CC Docket No. 01-324, attached to Ex Parte Letter from Peter Keisler, Sidley Austin Brown & Wood (representing AT&T), to William F. Caton, Acting Secretary, FCC (filed Feb. 8, 2002) (AT&T has recently stated that it has not pursued a strategy of converting platform customers to its own facilities "to provide basic local residential service to customers anywhere in the country").

[116] Public Interest Statement at 38.

[117] *See, e.g.*, Brief of Appellants and Intervenor at 3, *WorldCom, Inc. v. FCC*, No. 01-1198, *et al.* (D.C. Cir. filed Apr. 22, 2002).

[118] Public Interest Statement at 17 n.24.

in the merged company's service area, the Commission should insist that such arrangements involve telephony exclusively over Applicants' facilities in their service areas.

Audit. To ensure compliance with each of these conditions, the Commission should impose – as it has in other mergers of comparable size – an annual, comprehensive audit, and it should initiate aggressive enforcement action for any failure to implement not just the spirit, but the letter of the conditions.

CONCLUSION

The proposed merger of AT&T and Comcast will harm the public interest unless it is granted only subject to the above stated conditions.

Respectfully submitted,

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